



**REVIEW OF THE
ST. LOUIS PUBLIC SCHOOL DISTRICT**

**From The Office Of State Auditor
Claire McCaskill**

**Report No. 2004-47
June 14, 2004
www.auditor.mo.gov**

AUDIT REPORT



Office of
Missouri State Auditor
Claire McCaskill

June 2004

This audit is the second of two reports related to the St. Louis Public School District's financial viability. The first report issued in February 2004 reviewed the factors causing the district's financial hardship and budget projections. This report's 11 findings focus on the internal controls over management and financial functions, the factors that may have led to the declining financial condition, and the impact on the district of various cost reduction strategies.

The district's financial condition remains poor

The district's declining financial condition resulted from a combination of declining state revenues and a lack of significant reductions in expenditures. In both fiscal years 2002 and 2003, the district's expenditures exceeded revenues, leaving the district with a \$12.3 million deficit at the end of fiscal year 2003. From 2003 to 2004, district officials reduced expenditures by \$41.4 million; however, expenditures are still projected to exceed revenues, leaving the district with a \$38.6 million deficit at June 30, 2004. If additional cuts are not made, the district is projecting a \$54.6 million deficit for fiscal year 2005. While both the 2003 and 2004 deficit budgets were not in compliance with state law, the state will not sanction the district as long as the district is improving its financial condition. (See pages 5 through 7)

District's non-instructional costs were higher than the peer average

The district expended 30 percent more per student on non-instructional costs - such as transportation, food services, and warehouse operations - than the average of nine peer districts of comparable size. Auditors found such costs could have been reduced sooner. (See pages 6 and 7)

District had 17 more public school buildings than the peer group average

Total district enrollment has steadily declined over the past 15 years by 12 percent, but auditors found no evidence district officials evaluated school building needs. Shortly after the current Board and administration took over, they closed 16 schools. The resulting school closures saved an estimated \$14.5 million, while classroom sizes remained within state standards. Even after the consolidation, 6 of the 26 schools that received students from a closed school had occupancy levels below 70 percent. Additional and ongoing analysis by the School Board is necessary to ensure the efficient use of school facilities. (See pages 7 through 9)

(over)

YELLOW SHEET

District needs a policy requiring competitive bids for service contracts

The district does not have a policy requiring competitive requests for professional services. Auditors found several examples in which competitive requests had not been sought, or the district did not have adequate documentation to support the selection process. In addition, the district did not always include appropriate criteria to provide a means to monitor the contractor's performance. (See pages 9 through 13)

Inefficient bus routes cost millions, despite available resources to modify routes

District officials were not using bus routing software – available to districts for at least 10 years and owned by the St. Louis School District since 2002. An anticipated \$5.6 million in cost savings in fiscal year 2004 is anticipated by using the software, which increased efficiency and reduced the number of buses needed. In addition, the district has started to enforce the provisions of the transportation service contracts and should continue to improve this oversight. (See pages 17 and 18)

Poor inventory tracking caused excessive overstocking in worn down warehouses

In the fall of 2003, the district contracted for warehouse services and expects to pay approximately \$400,000 less than previously paid. The inadequate, manual-tracking systems in the former warehouse system resulted in significant overstocking including \$5.4 million in unused textbooks, expired janitorial supplies, and large quantities of chemicals. The district should continue improving the tracking procedures. (See pages 18 through 21)

Salaries paid to top district administrators are higher than the peer district average

The salaries of top administrators do not appear reasonable. For example, the Chief Operations Officer's \$200,000 salary is 75 percent higher than the peer district average. In addition, should the district pay its new superintendent the average salary based on a compensation study they used, that salary will rank in the top four in the nation. (See page 25 through 28)

Inventories of fixed assets are not performed and records are not maintained

The district does not have adequate controls and procedures for property items valued at \$51 million. Surplus property along with some unneeded vehicles should be inventoried and either placed into operation or disposed of. In addition, the district should consider obtaining independent appraisals for the real estate property it is trying to sell. (See pages 28 through 31)

Other recommendations

The audit also includes recommendations related to budgets, board meeting minutes, and cell phone and travel expense policies. In addition, the district should consider establishing an internal audit function. When making cuts and trying to balance the budget, the need for an internal auditor is even greater.

All audit reports are available on our website: www.auditor.mo.gov

REVIEW OF THE
ST. LOUIS PUBLIC SCHOOL DISTRICT
TABLE OF CONTENTS

		<u>Page</u>
	STATE AUDITOR'S REPORT	1-3
	MANAGEMENT ADVISORY REPORT - STATE AUDITOR'S FINDINGS.....	4-36
<u>Number</u>	<u>Description</u>	
1.	Financial Condition.....	5
2.	School Closing Analysis and Planning Procedures	7
3.	Contracting Issues	9
4.	Budgeting and Financial Management.....	13
5.	Transportation Operations	17
6.	Warehouse Operations and Inventory Tracking.....	18
7.	Administrative Expenditures	21
8.	Personnel Issues	25
9.	Fixed Assets and Surplus Property	28
10.	Board Minutes, Meetings, and Policies	31
11.	Internal Audit	34
	Response Letter From Prior Superintendent.....	35-36
	HISTORY, ORGANIZATION, AND STATISTICAL INFORMATION.....	37-43

STATE AUDITOR'S REPORT



CLAIRE C. McCASKILL
Missouri State Auditor

Honorable Bob Holden, Governor
and
Board of Education of St. Louis Public School District
801 Locust Street
St. Louis, Missouri

The State Auditor was requested by the Honorable Bob Holden, Governor, under Section 26.060, RSMo 2000, to audit the St. Louis Public School District. The district had engaged Rubin, Brown, Gornstein and Company, LLP, Certified Public Accountants (CPA), to audit the district's financial statements for the year ended June 30, 2003. To minimize duplication of effort, we reviewed the report and substantiating working papers of the CPA firm. The scope of our audit of the district included, but was not necessarily limited to, the year ended June 30, 2003. The objectives of this audit were to:

1. Review internal controls over significant management and financial functions and review compliance with certain legal provisions.
2. Identify any factors that may have led to the district's declining financial condition in the general operating funds.
3. Review cost reduction strategies and assess their impact on the district.

To accomplish these objectives, we reviewed minutes of meetings, written policies, financial records, and other pertinent documents; interviewed various personnel of the district, as well as certain external parties; observed district facilities; obtained comparative data from external sources; and tested selected transactions. Our methodology included, but was not necessarily limited to, the following:

1. We obtained an understanding of the financial accounting system and financial statements.
2. We obtained an understanding of internal controls significant to the audit objectives and considered whether specific controls have been properly designed and placed in operation. However, providing an opinion on internal controls was not an objective of our audit and accordingly, we do not express such an opinion.

3. We obtained an understanding of legal provisions significant to the audit objectives, and we assessed the risk that illegal acts, including fraud, and violations of contract, grant agreement, or other legal provisions could occur. Based on that risk assessment, we designed and performed procedures to provide reasonable assurance of detecting significant instances of noncompliance with the provisions. However, providing an opinion on compliance with those provisions was not an objective of our audit and accordingly, we do not express such an opinion.
4. We reviewed various aspects of district operations including, but not limited to; the board office, school closing criteria and methodology, the award and execution of significant consultant and outsourced operations contracts, district inventories and transportation department operations.

Our audit was conducted in accordance with applicable standards contained in *Government Auditing Standards*, issued by the Comptroller General of the United States, and included such procedures as we considered necessary in the circumstances.

The accompanying History, Organization, and Statistical Information is presented for informational purposes. This information was obtained from the district's management and its audited financial report and was not subjected to the procedures applied in the audit of the district.

The accompanying Management Advisory Report presents our findings arising from our audit of the district.

An additional report, No. 2004-09, *St. Louis Public School District Review of Financial Condition and Projections*, was issued on February 2, 2004.



Claire McCaskill
State Auditor

March 26, 2004 (fieldwork completion date)

The following auditors participated in the preparation of this report:

Director of Audits:	Thomas J. Kremer, CPA	
Audit Manager:	Alice M. Fast, CPA	
In-Charge Auditor:	Robert E. Showers, CPA	
Audit Staff:	Martin Beck	Kate Petschonek
	Kenneth M. Allman	Darrick Fulton, CPA
	A. Ash	

MANAGEMENT ADVISORY REPORT -
STATE AUDITOR'S FINDINGS

REVIEW OF THE
ST. LOUIS PUBLIC SCHOOL DISTRICT
MANAGEMENT ADVISORY REPORT

1.	Financial Condition
-----------	----------------------------

Despite the reductions made to the general operating budget in the current year, the district's financial condition remains poor. As discussed in our previous audit report No. 2004-09, *St. Louis Public School District Review of Financial Condition and Projections*, general operating fund expenditures exceeded revenues by \$13.5 million and \$49.4 million in fiscal years 2002 and 2003, respectively, resulting in an unrestricted general operating funds balance of negative \$12.3 million at the end of fiscal year 2003. As detailed in our prior report, the district's declining financial condition has resulted from a combination of declining state revenues and a lack of significant reductions in expenditures. As a result of the district's financial condition, the Department of Elementary and Secondary Education (DESE) designated the district to be "financially stressed" for fiscal year 2004, which requires the district to take action to correct its financial difficulties.

The following table depicts actual fiscal year 2003 financial information, as well as the revised 2004 budget information and 2005 budget projections (dollars are shown in millions):

		2004 Revised Budget¹	2005 Status Quo Projection²
	2003 Actual		
Beginning Balance	\$ 39.7	(12.3)	(38.6)
Revenues	356.3	338.0	332.1
Expenditures	(405.7)	(364.3)	(348.1)
Adjustment for Inventory Balance ³	(2.6)	NA	NA
Ending Balance	\$ (12.3)	(38.6)	(54.6)

The \$41.4 million net reduction in expenditures from 2003 to 2004 has resulted from numerous actions taken by current district management including closing 16 schools, contracting for many non-instructional services including maintenance, warehousing, and food service, reducing the number of administrative positions, and revising bus routes. However, even after these reductions, expenditures are still projected to outpace revenues by approximately \$26 million in fiscal year 2004, resulting in an expected ending general operating funds balance of negative \$38.6 million.

The current board and administration have received permission to borrow desegregation funds of up to \$49.5 million to cover any negative balance at the end of fiscal year 2004.

¹ As approved by the Board in February 2004.

² As presented to the Board in January 2004.

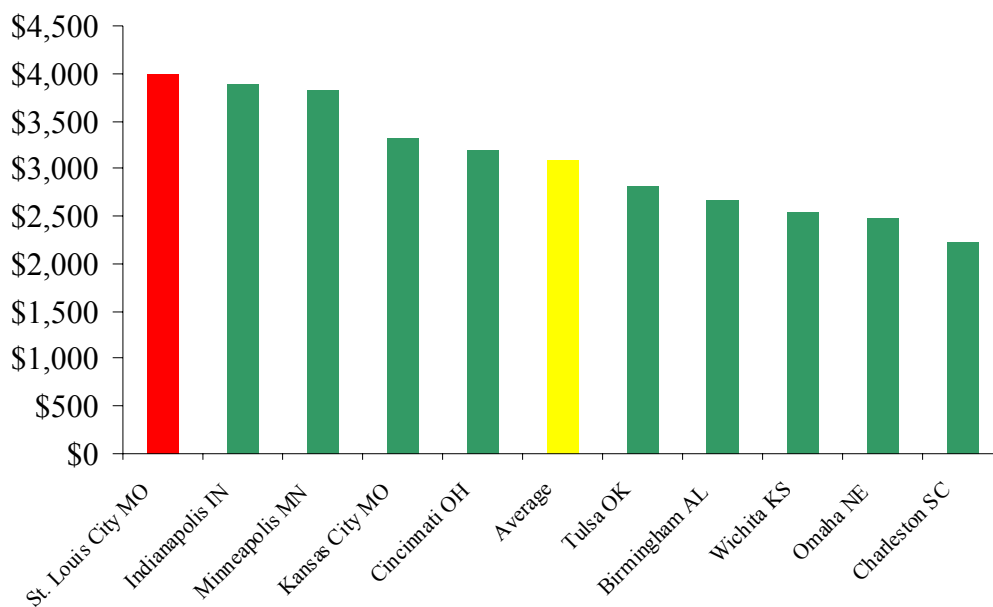
³ Adjustment for inventory balance at year end to show the ending unrestricted operating funds balance only.

Per court agreement, this loan is to be repaid in six annual installments, with a minimum annual payment of \$7 million, and is interest free.

For fiscal year 2005, with no additional cuts, the district is currently predicting expenditures will exceed revenues by approximately \$16 million; not including the first required \$7 million payment to replenish the desegregation fund. The result is a \$23 million deficit for fiscal year 2005. Since the desegregation monies will not be available in 2005 for general operating purposes, the district has no option but to eliminate this deficit. In March 2004, the Board began discussions on how to close this budget gap; however, even if the \$23 million deficit is eliminated, the district will still have a general operating fund balance of negative \$31.6 million as a result of the outstanding desegregation fund loan.

Data was obtained to determine how district spending compared to other districts of similar size and type. We obtained comparative data from the National Center for Education Statistics for nine peer districts which were selected based on enrollment levels (ranging from 38,000 to 48,000 students), classification (central city/urban), and general geographic area (midwest/south). The districts selected were: Birmingham, Alabama; Charleston, South Carolina; Cincinnati, Ohio; Indianapolis, Indiana; Kansas City, Missouri; Minneapolis, Minnesota; Omaha, Nebraska; Tulsa, Oklahoma; and Wichita, Kansas. The data obtained was for fiscal year 2002 and, therefore, does not reflect any current year reductions. According to the peer data, the district expended \$8,507 in total operating costs per student,⁴ or 16 percent more than the peer average. This higher spending per student was caused, in part, by the higher spending by the district on non-instructional expenses. According to the peer data, the district expended 30 percent more per student on non-instructional costs than the peer average. Non-instructional costs of the peer group are depicted in the following graph:

Non-Instructional Spending per Student



⁴ Total operating costs excluding capital expenditures and debt (\$374,042,000) divided by total enrollment (43,969).

Non-instructional expenses are those expenses not directly related to the classroom, such as administration and operations. As discussed further in this report, there are several areas in which non-instructional expenditures could have been reduced sooner to help improve the district's financial position. These areas include transportation (see Management Advisory Report (MAR) 5), food service (see MAR 3(D)), and warehouse operations (see MAR 6).

WE RECOMMEND the School Board continue to take appropriate action to ensure the long-term stability of the district's financial condition and ensure the district will be able to meet its obligation to repay borrowed desegregation funds.

AUDITEE'S RESPONSE

We concur with the recommendation and have worked this past year and will continue to work toward that goal with an extensive set of plans and programs to bring expenses in line with revenues for the 2005 academic year. These plans and programs have been and will continue to be public records.

A comprehensive program of options to accomplish additional expense reductions was developed during the past several months for the Board, community, and employees to discuss and give feedback. These options included reductions in personnel levels through attrition, coupled with possible other reductions in force, and modifications in benefit costs. A hiring and salary freeze is in place and the possibility of reductions in salaries was considered. Possible reductions in programs outside the core K-12 curriculum were considered also.

The Board has approved a voluntary retirement incentive program that would encourage employees eligible for retirement to retire at the end of this school year as a means of supplementing normal personnel attrition. The success of this program will dictate to some extent the need to pursue other expense reduction programs in an effort to balance expenses and revenues for the 2005 General Operating Budget.

2. School Closing Analysis and Planning Procedures

Prior administrations have failed to adequately monitor enrollment and demographic data to reexamine the district's school facility needs. Even with declining enrollment, there is no evidence the district was reviewing and evaluating school building needs. Total district enrollment has steadily declined over the past 15 years a total of 12 percent. More specifically, enrollment in the northern portion of the district has decreased 40 percent while enrollment in the southern portion of the city has increased 42 percent. Despite these significant changes in enrollment patterns, district planning personnel indicated the district *added* a net of seven schools over this time period and only one of those net schools was constructed in the southern portion of the district.

Data obtained from a peer group of nine other school districts similar to St. Louis (see MAR 1) indicates that the number of school buildings in operation in St. Louis (prior to the closures in the summer of 2003) was 17 more than the peer group average.

The current Board and administration took action to close 16 schools immediately prior to the 2003-2004 school year, with the anticipated savings from the closures estimated to be at least \$14.5 million. The number of district school buildings before and after school consolidation, by region, is as follows:

Region	2002-2003	2003-2004	Difference
	School Year	School Year	
North	55	43	(12)
Central	18	15	(3)
South	36	35	(1)
Total	109	93	(16)

The consulting firm that performed the school closing analysis used a standard methodology and criteria, similar to analyses performed by them in other districts. The evaluation criteria were:

- Schools with a high percentage of unused classroom space (70 percent occupancy or less).
- Space available in nearby school buildings.
- Buildings that accommodate 300 students or less.
- Schools not constrained by the desegregation settlement order.
- No planned housing starts in the vicinity of the school.
- Low educational performance, as measured by test scores.
- Buildings that have not been renovated.
- Older buildings with high maintenance costs.
- Buildings that are due for expensive maintenance or renovation within the next two years.

Based on our review, the stated methodology and criteria were consistently applied and the resulting school closures resulted in classroom sizes remaining within state standards.

Additional analysis is necessary to ensure school facilities are used in an efficient manner. Even after the consolidation, 6 of the 26 schools that received students from the closed schools had occupancy levels below 70 percent, the preferred occupancy level as defined in the closing criteria. With predictions of declining enrollments, continuing financial difficulties, the impact of charter school enrollment, and the possibility of an influx of students returning to the district due to the end of the desegregation agreement, additional and ongoing analysis by the School Board is necessary to ensure the efficient use of school facilities.

See MAR 9 for discussion regarding the sale of closed school property.

WE RECOMMEND the School Board perform ongoing enrollment and demographic trend analyses to ensure efficient use of school facilities.

AUDITEE'S RESPONSE

We concur with the findings and recommendations.

The Board will continue to analyze facilities needs using the same methodology as used in July of 2003.

3. Contracting Issues

The district does not have a policy requiring competitive requests for proposals for professional services. Some contracts did not have adequate documentation to support the selection process and some contracts provided little or no monitoring criteria to allow for the evaluation of the services provided. In addition, the food services contract should be monitored to ensure financial expectations are met and past losses are not repeated.

A. There were no requests for proposals for several service contracts.

- Alternative education services totaling approximately \$2.7 million per year for fiscal years 2002, 2003, and 2004 were contracted for without requesting proposals.
- Labor negotiation and human resource consulting services totaling \$510,000 were contracted for in August 2003 without requesting proposals.
- Purchasing coordination services to provide an on-line supply ordering system totaling \$125,000 were contracted for in October 2003 without requesting proposals.
- Accounting and consulting services to review the management team's financial projections in the amount of \$33,600 (160 hours of work at \$210 per hour) were contracted for in August 2003 without requesting proposals.
- Two separate educational consulting services contracts, one for \$78,750 and the other for \$150,000, for programs intended to help improve test scores and motivation were entered into in August 2002 and October 2002, respectively, without requesting proposals.
- A contract for employee health benefit management and administration services estimated to cost \$4.3 million annually was awarded in November 2003 without proposals being requested. This contract provides for online benefit enrollment and customer service as well as benefit management

services. Services include contract negotiations, monitoring of benefits usage, and implementation of programs to reduce future claims and costs.

See MAR 8 for additional concerns regarding benefits.

A formal written policy requiring competitive requests for proposals for all service contracts is necessary. While professional services may not be subject to standard bidding procedures or required by state law, it is good business practice to solicit proposals for such services and select the best proposal based on cost, experience, the type of service to be provided, and any other relevant factors.

B. The district did not maintain adequate documentation of the selection process for some contracts or did not adequately evaluate some contract proposals.

- District management services to be completed during fiscal year 2004 up to \$4.5 million plus expenses of up to \$330,000 and performance audit services in the amount of \$500,000 plus expenses were contracted for in the same contract in July 2003. The performance audit aspect of the contract was later increased by the Board to \$920,000 due to an increase in the scope of work, including consulting on outsourcing services. Although there was some evidence that the district used a selection process, the process was not adequately documented. The district received ten responses to its nationally advertised request for proposals for these services from firms with various experience levels and backgrounds. Eventually, the selection committee decided on one management firm and another firm was selected to complete the performance audit and consulting work. Due to potential overlaps in the services to be provided, the district combined the management services and performance audit services into one contract. Even though the request for proposals had evaluation criteria, the manner in which the selection committee narrowed the field for both services and made their final selection was not documented. With no documentation of how the proposals were evaluated, there is no justification of why these firms were selected over the other firms.

See additional comments regarding the reasonableness of expenses charged under this contract at MAR 7.

- Bond underwriting services of \$897,000 were contracted for in April 2003. The district did not advertise for proposals outside the city of St. Louis, only advertised in two local papers with limited circulation, and received only two proposals with one of them being \$200,000 higher than the other. The district presented reasons for the selection of the higher bidder; however, the selection process used did not include cost as part of the evaluation criteria. District personnel indicated cost was not originally a criteria because the issuance costs were going to be paid through a state program. However, the state funding did not materialize and the district will be liable for the full cost of these services.

- Supply warehouse services, including inventory receiving, delivery, and tracking services, were outsourced at an annual cost of approximately \$400,000 in August 2003. These services were not formally advertised, but according to the consultant involved in the process, they "let it be known" that the district was in the market for such services. The consultant indicated they received proposals from three vendors and, because the winning proposal was adequate and much cheaper than the other proposals, a formal evaluation process was not completed. However, without formally requesting proposals and establishing the work required, there is no way to ensure proposals are comparable in services proposed. A lower cost could indicate less service. We were unable to determine if the proposals were for comparable services because the district could not locate the documentation of the proposals received.

See additional concerns regarding the warehouse operations at MAR 6.

- The selection process for payroll processing and time tracking services was completed during fiscal year 2004. Although requests for proposals were not formally advertised, several vendors made presentations and were interviewed by district personnel. It was not clear how the final vendor was selected because written proposals and evaluations could not be located. At the time of our review, contract terms had not been finalized, but these services are expected to cost approximately \$600,000 annually.
- Computer consulting and training services of \$69,439 were contracted for in November 2002. These services were for the implementation of the district's financial accounting software. District personnel in the technology section indicated that several proposals were received for these services; however, no documentation of such proposals could be located. Purchasing section personnel indicated the district did not advertise for proposals.

To ensure the district is selecting the best service provider at the best cost, the selection criteria must include cost and the selection process must be fully documented.

- C. The district did not always include monitoring criteria and/or monitor service contracts effectively. Some contracts had monitoring criteria which were vague or non-existent.
- The contracts for alternative education services, mentioned in part A, contain no performance assurances or measurement criteria to ensure the district is getting quality services. These contracts are in their third and final year and have yet to be formally evaluated. District officials indicated that they have plans to evaluate the programs but have not found the time to do so.

- The \$150,000 educational consulting contract, mentioned in part A, contains minimal performance criteria. This contract was to provide services to five middle schools with stated objectives of improving student motivation and increasing academic achievement. While the teachers participating in this program completed an evaluation form for the program, it does not appear that any formal assessment was performed to determine the effectiveness of the program.

By not including clearly defined expectations and methods for measuring contract results, and periodically evaluating the results, the district does not know if the services received are meeting their needs. Service contracts should provide that the contractor deliver clearly defined results that can be measured and used to hold the contractor accountable for quality and reliable services.

- D. Food service operations have operated at a loss for several years. According to the district's audited financial statements, food service expenditures have exceeded revenues by approximately \$6 million from fiscal year 2001 to fiscal year 2003. Even though expenditures remained relatively constant over that time period, revenues were not enough to cover the costs, due in part to the low participation rate of students in the meal program. This rate for high school students is currently 25 to 30 percent. Revised budget projections anticipate expenditures will exceed revenues by approximately \$1.8 million in fiscal year 2004, as well. Deficits of the Food Service Fund must be subsidized by the general operating funds, which has added to the financial difficulties of the district.

In an attempt to improve efficiency, food service operations were outsourced in March 2004. The food service contractor has guaranteed the Food Service Fund will generate surpluses of \$1.4 and \$1.6 million in fiscal years 2005 and 2006, respectively, through increased participation and upgraded facilities. The contractor believes they can increase participation and serve one million more meals each year. While no problems in the process used to award the food service contract were noted, the district should monitor this contract closely to ensure contract conditions are met and guarantees are received.

WE RECOMMEND the School Board:

- A. Adopt a policy which requires competitive requests for proposals for the purchase of services.
- B. Maintain documentation detailing all proposals received, the selection criteria used, and the reason for selecting the final proposal. Cost should be a criteria in all selections.
- C. Ensure service contracts include appropriate criteria which provide a means to monitor the contractor's performance.

- D. Continue to monitor the food service contract to ensure contract conditions are met and guarantees are received.

AUDITEE'S RESPONSE

- A. *State statutes do not require competitive requests for proposals for the purchase of services.*
- B. *St. Louis Public Schools (SLPS) agrees that it is important to maintain documentation detailing all proposals received, selection criteria, and reasons for selection of a particular firm. Cost should be one of the criteria in all selections but not necessarily the only criteria. Quality of service, experience and other factors should also be considered. Board procedures will be developed and adopted by September 2004 to assure standardization of the recommendation.*
- C. *All major service contracts will include measures or metrics to monitor performance of the contractors. Major contracts constitute, Buildings and Grounds (Sodexo), Food Service (Aramark), Transportation (Laidlaw), and Health Benefit Management (Mercer). Performance metrics are in place for Sodexo and others will be in place by September 30, 2004. In the next twelve months the Board will craft and adopt a policy that establishes requirements whereby major contracts are assessed quantitatively and qualitatively.*
- D. *The food service contract will be monitored monthly to ensure contract conditions are met and guarantees are received.*

AUDITOR'S COMMENT

- A. Although not required by state law, soliciting proposals for professional services and selecting the best proposal based on cost, experience, and any other relevant factors, is a sound business practice.

4. Budgeting and Financial Management
--

Previous boards did not get the information needed to adequately monitor the budget and the district's financial position. In addition, significant audit adjustments were needed at year end due to the inaccuracy of the district's financial information, original budgets

approved by the prior Board contained unreasonable estimates and required significant revision, and the district budgeted deficit balances. The prior administration did not adequately monitor and project cash balances of district funds.

- A. Budgetary procedures were not sufficient to provide board members with the information needed to adequately monitor the budget and the district's financial position prior to fiscal year 2004, as discussed in our previous audit report No. 2004-09, *St. Louis Public School District Review of Financial Condition and Projections*. In addition, the Board did not adequately review proposed budget amendments. Financial information, including budget amendments, presented to the Board by the district administration did not include the effects of the amendments on the operating funds ending balance. The amendments did not always contain information adequate enough to explain the reason the increase was necessary. There is no documentation that indicates the Board received monthly updates on the status of the general operating funds balance or reserve. In addition, no comparison was made of budget to actual revenue numbers. Without such information, the financial status of the district and the magnitude of the financial crisis could not be appropriately assessed.

During fiscal year 2003, the Board approved approximately \$12 million in additional appropriations through budget amendments without adequate information giving the reasons for the increases and the impact of the increases on the district's financial position. It is the responsibility of the Board to ensure they are being provided the appropriate level of information to allow them to monitor the overall financial picture of the district.

During fiscal year 2004, the Board has been provided more timely financial information and projections. This information should allow the Board to monitor the financial position of the district and plan future budget adjustments.

- B. Inaccuracies in financial information provided to external auditors, such as unrecorded accounts payable, resulted in significant audit adjustments to the fiscal year 2003 and 2002 financial statements at year end. These audit adjustments, when made, resulted in actual expenditures exceeding budgeted expenditures in fiscal years 2002 and 2003, as follows:

Fiscal Year	Adjusted Budget	Actual Expenditures	Expenditures over Adjusted Budget
2002	\$ 387,764,473	390,937,116	3,172,643
2003	401,871,462	405,763,152	3,891,690

Section 67.080, RSMo 2000, provides that no expenditure of public monies shall be made unless it is authorized in the budget. However, the effectiveness of the budgeting tool is minimized when the financial information used is not accurate. Ensuring the accuracy of financial information throughout the year would

minimize the need for such adjustments and would allow the Board and district administrators to more accurately monitor district operations.

- C. The original fiscal year 2003 budget approved by the Board contained unreasonable estimates which were not based on historical information and required significant revision. Several of the amendments were for items that were not unforeseen circumstances and the stated purpose of many of these amendments was to "restore prior year's budget". Because these additional appropriations were approved early in fiscal year 2003, they appear to be a result of inadequately planned cuts to the original fiscal year 2003 budget. For example, budgets for heating and electric costs were reduced from prior year levels when there was no apparent basis for doing so. As a result, the Board approved \$1.6 million in additional appropriations to pay utility bills. Also, approximately \$2.7 million in additional appropriations were necessary to budget for alternative education contracts; however, these contracts existed in the prior year and should have been included in the original budget.

A complete and well planned budget serves as a useful management tool by providing management with an effective means to monitor specific cost expectations. An incomplete budget hampers management's ability to accurately monitor costs.

- D. The district's current budget projects a deficit general operating funds balance at June 30, 2004. In addition, in fiscal year 2003, although a deficit was not originally budgeted, the year end general operating funds balance was negative \$12.3 million. Section 67.010 (2), RSMo, requires all political subdivisions to have a balanced budget. However, it will require some time for the district to recover from its current financial situation and reasonably balance its budget to achieve statutory compliance. As noted in MAR 1, the district's projected budget for fiscal year 2005 also results in a negative operating funds balance. Per DESE, as long as the district continues to make progress towards improving their financial condition, no sanctions will be prescribed against the school district for having a negative operating funds balance. The district must continue to make the necessary changes to ensure a balanced budget in future years.
- E. The district administration did not adequately monitor and project cash balances of district funds. As discussed in our previous audit report No. 2004-09, ***St. Louis Public School District Review of Financial Condition and Projections***, the prior administration was not aware that general operating fund cash balances fell below zero during fiscal year 2003. The district maintains a pooled or combined bank account which includes several funds including the general operating funds, desegregation, federal, and other restricted funds. In December, when the general operating funds were negative, the other funds with positive balances covered the negative cash amount. The current administration has implemented processes to actively monitor and project cash balances. This allows the district to more effectively manage and plan its cash needs.

WE RECOMMEND the School Board:

- A. Ensure they continue to receive adequate financial information to allow them to appropriately monitor the district's financial condition and approve budget amendments only after reviewing information that explains the reason for the amendment and the effect of the amendment on the district's financial position.
- B. Ensure district financial information is more accurately prepared to minimize year end audit adjustments.
- C. Thoroughly develop budgets to ensure additional appropriations are only necessary for unforeseen circumstances.
- D. Continue to work towards balancing the budget.
- E. Continue to monitor and project the district's cash balances on an ongoing basis.

AUDITEE'S RESPONSE

We concur with the recommendations.

During the 2004 fiscal year a set of major improvements has been implemented with respect to financial tracking, analysis, and reporting of actual financial results compared to budgeted results on a monthly basis. This includes a series of detailed reports which track the General Operating Budget performance relative to budget by revenue and expense class as well as by functional area. These reports are used by the administration to track expenses on a monthly basis relative to budget. These same reports are used to forecast the balance of the year and to determine steps to be taken to remain on budget. These reports are provided to district management on a monthly basis for review and follow up.

A cash flow forecasting and tracking system was also implemented which provides for a rolling 13 week forecast of current and expected cash positions. This system is currently being enhanced to provide longer-term full year cash forecasting capability to provide adequate monitoring of liquidity in order to plan in advance for future needs.

Both of these reports are summarized and presented to the Board on a monthly basis showing a comparison of budget to actual, forecasting full year expected financial performance, and analyzing any major variances to budget. In addition to these reports, a five year financial forecast is being developed to provide a more comprehensive longer term view of the financial status of the district.

Deficiencies and weaknesses were noted regarding the district's transportation operations including the failure to efficiently plan bus routes in the past and the lack of adequate monitoring of performance aspects of the bus vendors' contracts.

The district paid three bus contractors a total of \$28.5 million in fiscal year 2003, and has budgeted to spend approximately \$22.9 million in fiscal year 2004, for to and from school bus services.

- A. Prior district administrators did not use available resources to efficiently plan bus routes. The district is anticipating cost savings of \$5.6 million on contracted transportation in fiscal year 2004 compared to fiscal year 2003. District administrators indicated that a portion of this savings can be attributed to more strict adherence to board transportation policies; however, the majority of the savings will be due to the implementation of bus routing software immediately prior to the 2003-2004 school year which increased efficiency in the bus routes. The number of buses in daily operation was reduced from 568 in 2003 to 427 in 2004. DESE transportation personnel indicated that routing software has been available for approximately 10 years. While this software had been purchased during fiscal year 2002, it had not been placed in operation by the district and, until fiscal year 2004, the district manually mapped bus routes and bus stops. District transportation personnel offered no explanation as to why such software had not been implemented sooner. The new software also includes features to enable the district to ensure compliance with state rules and safety regulations regarding the length of time a student is on a bus, the number of students on a bus, the location of bus stops, and the routes students must walk to get to bus stops.
- B. The district did not adequately monitor the performance aspects of the primary bus transportation vendor contracts. While these contracts contained stipulations for the vendors to ensure contract performance, equipment maintenance, and driver certifications, the district produced no documentation showing how it actively monitored for such compliance. A lack of monitoring can lead to substantial non-compliance and a lack of adequate service.

The district is in the process of restructuring the primary bus transportation contracts in an effort to improve the quality of services received. The proposed transportation contracts are more specific in terms of damages the contractors must pay in the event of contract non-compliance such as late arrivals, safety violations and driver certifications. To help enforce these contract stipulations, the district created a field supervisor position during fiscal year 2004. The proposed contract will also require contractors to make specific safety upgrades to their equipment within specified time periods, such as digital video cameras and global positioning system transmitters. The district believes these improvements should help ensure it receives improved transportation services.

WE RECOMMEND the School Board:

- A. Continue to improve efficiency in routing buses under contracted transportation.
- B. Improve its oversight of transportation contractors to ensure compliance with agreed upon contracts.

AUDITEE'S RESPONSE

- A. *We agree with the auditor's recommendation to continue to improve efficiency in routing buses under contracted transportation.*
- B. *The district is moving to a single source for transportation outsourced services. This will allow for:*
 - *Only one party to manage instead of multiple.*
 - *Quicker response for any instance since the focus will be on one contractor.*
 - *More centralized control of the operations.*
 - *Less confusion regarding which company causes any concern.*
 - *Easier accounting of service.*
 - *More control over excess time and activities.*
 - *Better communication regarding changes of routes or times.*
 - *Consistency in billing, management, and response.*
 - *Consistency in company policy.*

6. Warehouse Operations and Inventory Tracking

Prior to fiscal year 2004, the district maintained two warehouses and rented space at a third storage facility. The warehouses maintained by the district were of poor quality and the systems in place to track and locate supply inventories were not adequate. In addition, a cumulative inventory of textbooks was not maintained. In the fall of 2003, the district contracted for warehouse services. As a result, one of the district's two warehouses is currently for sale and the district no longer rents space at the third facility. Instead, all inventory is stored at the contracted services' warehouse. The other district owned warehouse is currently being used to store surplus property.

The district expended approximately \$838,000 on warehouse operations in fiscal year 2003, and in fiscal year 2004, the district expects to pay for contracted warehouse services of approximately \$400,000. As of December 31, 2003, total inventories in the warehouse were valued at \$7.8 million.

- A. Inventories were tracked using a manual process where personnel at district headquarters updated the inventory records based on manual communications from the warehouse. This manual process combined with a lack of physical inventories being conducted, led to the district's external auditors noting

"significant discrepancies" between physical counts and inventory records. The poor condition of the warehouses, such as broken elevators and unclearly marked items, combined with the inaccuracies in the inventory records, resulted in the district not being able to adequately and timely deliver supplies to the schools. Maintaining an accurate inventory is also essential to an efficient purchasing and procurement process.

In an effort to address the weaknesses noted above, the district outsourced warehouse operations early in fiscal year 2004 to a professional warehousing company. The outsourced warehouse uses a perpetual inventory system where the inventory records are immediately updated when an item is placed into, or taken out of, inventory. The district is also in the process of refining their supply ordering and procurement process to allow orders from the schools to be made electronically to the district procurement office and on to the warehouse.

- B. Due to the district's inadequate tracking system, inventory levels were not adequately monitored for reasonableness, resulting in significant overstocking of some inventory items. For example, as of December 31, 2003, the district maintained a textbook inventory in the warehouse valued at \$5.4 million. These are extra books that have never been used and are not needed for immediate use in the schools. During our visit to the warehouse, we observed various other overstocked items, such as janitorial supplies. According to the district's Chief Operating Officer, many of the janitorial supplies on hand cannot be used because they are past their expiration dates and must be taken out of inventory. We also observed several other supply items in inventory that appeared to be overstocked, such as 21 heavy pipe wrenches (over a one year supply) and a total of 160,000 sheets of 18X24 green construction paper (approximately a year's supply). In addition, we noted dangerous chemicals including 108 bottles of sulphuric acid and 117 bottles of hydrochloric acid. According to contracted warehouse and Department of Natural Resources personnel, such chemicals should not be warehoused, especially in such high quantities.

The overstocking of inventory is an inefficient use of district funds. In addition, many businesses can now deliver supplies as needed, eliminating the need to warehouse supplies in any quantity. Money spent on unnecessary inventory could be used to fund other aspects of district operations. Overstocked inventory also takes up unnecessary warehouse space, which must be taken into account now that the district's contracted warehouse costs are based on square footage of space used.

- C. The district did not maintain a cumulative inventory of unused textbooks. While the district had approximately \$5.4 million in new unused textbooks recorded in inventory in the warehouse as of December 31, 2003, an unknown amount of additional textbook inventories existed at the school level due to each school's use of "textbook banks" where surplus textbooks were kept. These books are extras that the school has received from the warehouse but does not need for classroom

use at this time. Inventories are not maintained of each school's "textbook bank" or of the books in use. In March 2004, the district performed a count of all textbooks located at the schools and determined that between the schools and the warehouse, the district had over 693,000 books valued at approximately \$15.5 million. By not maintaining a cumulative textbook inventory, the district has no way of ensuring all textbooks on hand are being used prior to ordering new ones.

WE RECOMMEND the School Board:

- A. Continue to improve inventory tracking procedures to ensure accurate inventory records. Physical inventories should be conducted periodically.
- B. Monitor inventory levels and reduce inventory to reasonable levels of usage.
- C. Prepare and maintain a cumulative textbook inventory to ensure efficient use of textbooks.

AUDITEE'S RESPONSE

- A. *The district will continue to improve its inventory procedures and logistics policies.*
- B. *It is agreed that money spent on inventory that is ultimately not used is a missed opportunity to direct that capital to the needs of schools. SLPS is focused on reducing inventory across all channels including textbooks. For example, the district no longer purchases janitorial supplies, which was one of our aged inventory items. Instead Sodexo, our Buildings and Grounds contractor, now sources these items. SLPS is also investigating if some of this inventory can be resold or restocked to further reduce our present inventories.*
- C. *Following the report by the Council of Great City Schools on textbook deficiencies, SLPS launched a textbook project to inventory textbooks and identify requirements for the next school year. Past practices have been inconsistent and resulted in the significant over ordering of textbooks in some cases and in other cases some students potentially not having the needed textbook for their classes. As an example, it was a regular practice in the past to order approximately 10 percent overages each year for textbooks. This practice has resulted in significant inventory that is not used. This present warehouse inventory of unused textbooks is estimated at \$5.4 million. The textbook project has the following goals and objectives:*

PURPOSE:

- 1. *The Textbook Inventory/Procurement Project Team will conduct a detailed, physical inventory of all textual material currently being utilized by SLPS. (Last year SLPS expended approximately \$9.8 million on textual materials. This year SLPS has a maximum of \$3.7 million to satisfy our needs).*

2. *The Textbook Inventory/Procurement Project Team will conduct a detailed, review of the 2,600 titles of the textual material catalogue and reduce the number of titles to 800 (via identification of obsolete or discontinued titles).*
3. *The Textbook Inventory/Procurement Project Team will ensure that required textbooks and instructional materials will be provided to students by the first day of school without ordering excess inventory.*

DELIVERABLES:

- *Assessment of textbooks in stock at schools.*
- *Assessment of textbooks in Madison Warehouse.*
- *Develop a process for scanning in bar codes of textbooks.*
- *Develop a process for redistribution of textbooks among schools.*
- *Develop a process for ordering textbooks.*
- *Develop a process for distributing newly ordered and refurbished textbooks to schools.*
- *Develop a process for ongoing textbook management (textbook operations manual) throughout the District.*

7. Administrative Expenditures

The Board failed to adequately ensure management services expenses stayed within limits specified in the original contract, cellular phone usage was not adequately monitored, and travel expense reimbursement policies and procedures were not adequate.

- A. The Board did not effectively monitor and limit travel and lodging expenses incurred by the management team. The original contract for management services contained a travel and lodging expense limit of \$330,000, with fees limited to \$4.5 million. However, in April 2004, at the request of the management team, the Board voted to eliminate the original travel expense limit, as long as total expenses and fees did not exceed the original combined contract amount of \$4.8 million. Through April 2004, the management team had accrued \$3.8 million in fees (approximately 11,400 hours) or 84 percent of the maximum and had billed the district for approximately \$341,000 in travel expenses. There is no documentation explaining why travel expenses are exceeding the maximum limit while it would appear such expenses should closely correlate to the fee expense.

While the overall travel expense limit was eliminated, the contract does specify that the management team is to be paid a \$50 per diem for meals and no more than \$125 per night for lodging which is in accordance with the district's informal travel policy for board members (see part C below). The contract also specifies that the management team will only be reimbursed for "the lowest rate ticket available for a direct flight" for airline tickets, taking into consideration the

necessary flexibility to perform their duties. However, by eliminating the limit on travel expenses, the Board limited its assurance that overall travel expenses incurred were reasonable and eliminated the management team's responsibility to contain their travel costs. While expenses were approximately within these specific contractual limits, it appears the management team could have done more to ensure it stayed within the original limit. For example:

- Members of the management team traveled to and from their homes on a weekly basis, incurring additional travel expenses charged to the district.
- The members of the management team rented furnished suites at a local hotel at a cost of \$1,900 per month for all the team members except for the Acting Superintendent who had a suite costing \$2,400 per month. Although these monthly rates compute to less than the \$125 nightly rate set by the contract, it is not evident why the Acting Superintendent needed a more expensive suite.
- An invoice submitted for reimbursement by the management team in the amount of \$5,050 for legal services for the preparation of their consulting contract with the district was submitted as an expense for reimbursement. The management team's contract with the district does not specifically identify legal costs as a reimbursable expense.

Travel expenses should correlate to actual time spent and fees charged. The district should expect contractors to not exceed original contract limits set without adequate explanations.

- B. The district does not have a formal written policy for cellular phones and pagers, including a restriction against personal use, and did not adequately monitor the phones in operation. During the year ended June 30, 2003, the district utilized five vendors and incurred costs of approximately \$141,000 for monthly services and equipment purchases for cellular phones, two-way radios, and pagers. The district entered into multiple contracts, many with the same vendor, to provide cellular phone and pager services. District officials did not know the number of cellular phones in use and did not have procedures to track to whom individual phones had been issued. The phones and pagers were issued primarily to various district departments, buildings, and personnel, but in most instances it could not be determined who actually used the equipment during the billing period.

Our review of cellular phone invoices noted the following problems:

- The invoices only provide detail of the calls requiring a roaming charge making it impossible to review for personal usage.
- Of the 79 phones included on one billing, 23 were used for less than 100 minutes each during the period and another 15 had no usage for the month (on a 600 minute plan). The total cost for these 38 phones for the billing period

was approximately \$1,550. Calling plans should be reviewed to ensure they fit the usage needed.

- Four individual phone charges exceeded \$100 each, with the largest amount being \$456 for a phone assigned to Dunbar Elementary School, which used a total of 2,347 airtime minutes, or an average of 78 minutes per day during the billing period, including 659 night and weekend minutes. Phone usage should be reviewed to ensure all calls are business related.

It appears that overall phone costs could be reduced by using the district's wired phones rather than cellular phones when possible. The Board should develop policies and procedures for cellular phone and pager usage. Usage of cellular phones and pagers should be monitored to ensure it is necessary and for district business only. The current district administration has taken steps to address these weaknesses by reassessing the necessity of each phone issued and consolidating cellular phone and pager service under one vendor.

- C. The district does not adequately monitor travel expenditures and does not have an adequate policy regarding reimbursable travel expenditures. The district expended approximately \$1 million for employee travel from all funds during fiscal year 2003. In addition to paying expenses through a reimbursement policy, the district also currently uses a travel advance process in which the employee receives prior approval for a trip and is given an advance prior to their departure. Upon returning, the employee is to submit all receipts documenting their actual expenses incurred. Any unused advance is to be returned to the district, or if expenses are incurred in excess of the advance, the employee is reimbursed. The district's policy, which was last amended in 1998, allows a \$30 per diem meal allowance and a maximum reimbursable room rate of \$125 per night. District personnel indicated that the meal per diem for Board members is informally set at \$50; however, this is not documented in the policy.

A review of nine travel advancements noted the following concerns:

- Expenses are not always claimed on a standard form and were, therefore, inconsistently documented. There was very little documentation to indicate the purpose or benefit of the trips.
- On four of the nine advances reviewed, the individual failed to provide any documentation to support actual expenses. One instance involved a Board member who was advanced \$1,362 to attend a conference. The fiscal control section did not adequately follow up with these individuals.
- Daily meals were reimbursed at actual costs instead of the stated \$30 per diem rate, contrary to district policy. Actual meal costs incurred exceeded the per diem rate on at least one day on all five of the travel reimbursements that

submitted documentation. One board member reimbursement included an average of \$56 in meals claimed per day.

- On seven of nine travel advances/reimbursements reviewed, hotel accommodations exceeded the \$125 per night allowance with two of these instances involving Board members who paid \$176 and \$215 per night.

The use of travel advances creates administrative problems due to the time requirements to follow-up with individuals who have not turned in their documentation. The use of a travel reimbursement policy, in which major travel expenses (such as hotel, airfare and conference registration fees) are paid directly by the district and meal expenses are capped at a set amount and are reimbursed upon submission of an expense claim, would provide for better controls. Requiring travel expenses to be reported on a standard reimbursement form stating the purpose of the travel would allow for easier review of expenses and would help ensure expenses incurred are reasonable and for school district business. Maximum amounts allowable for reimbursement should be established based on the location of the travel and the reasonable costs at that location.

WE RECOMMEND the School Board:

- A. Include and follow strict limits on expenses to be allowed on any future contracts. Any changes in contract limits should be adequately explained.
- B. Establish a policy for cellular phone and pager use stating the individuals authorized to be assigned a phone or pager and the allowable use of the phones and pagers. All billings should be reviewed for reasonableness and the Board should ensure cell phones are used only for district business.
- C. Establish a comprehensive written travel policy outlining the types of expenses allowed, maximum amounts, and documentation, approval, and review requirements. The Board should consider eliminating the use of advances. Travel expenses should be reviewed to ensure policy requirements are met and that only necessary and reasonable charges are paid by the district.

AUDITEE'S RESPONSE

- A. *The Management Team's original contract was for \$4,804,300, which was comprised of an estimated \$4,474,300 of fees and \$330,000 of out of pocket expenses. Both the fee and expense amounts in the Management Team's contract were estimates based on the scope of work known at the time of the Management Team contract in May 2003. In April 2004, the Board approved a removal of the separate fee and expense caps on the Management Team's contract, while keeping the total cap of \$4,804,300 intact, leaving the total cost to the District unchanged.*

On June 3, 2003, the Management Team's scope of work significantly changed as a result of the prior Administration's reporting of the District's severe financial crisis. Despite this change in scope of work, the Management Team expects to charge the District significantly less than its contracted amount of \$4,804,300. The Management Team expects its cost to be under budget as a result of: (a) aggressively monitoring Management Team staffing levels and maximizing use of existing employee resources within the district (The Management Team utilized only two full-time employees for the last 2.5 months of its contract); (b) using discount airlines where possible; and (c) keeping nightly lodging expenses below its contracted allowance.

Every member of the management team abided by the contracted nightly rate of \$125 for lodging expenses. Although the Acting Superintendent's monthly apartment rent was more than other team members' rent, he was often required to stay weekends in St Louis as a result of his role on the engagement. Therefore, his nightly lodging expense was comparable, if not even less, than other team members, and certainly, it had no material impact on the total cost of the Management Team's contract.

With respect to the issue of the \$5,050 of legal expenses billed to the district by Alvarez & Marsal (A&M), the auditors determined it to be a non-reimbursable expense. The standard A&M contract requires the client to pay legal fees associated with the client's engagement letter. The final contract did not contain this clause. A&M did bill this amount, and were reimbursed. Upon discovering that this was not a reimbursable amount, the district and A&M agreed to reverse this charge and to account it against the hold back amount which is owed to A&M by the district.

- B. The State Auditor recommends, and the district agrees, that the district should have a policy for cell phones and pagers. Effective May 2004, the district adopted a communication device policy, defining approved users of communication devices and moving asset management and expense incurral under a centralized umbrella. Ultimately, the new district policy seeks to ensure the safety of its children, minimize costs and streamline communications.*
- C. The State Auditor recommends, and the district agrees, that the district should update the travel policy and should consider modifying the use of expenditure advances. The district intends to review and update this policy prior to the end of the calendar year.*

8. Personnel Issues

Several issues were identified regarding personnel matters including excessive administrative salaries and increasing health benefit costs.

- A. Current salaries of top district administrators are compared to peer school district averages in the following table:

Position	District Salary	Peer Average Salary	Percent Higher
Superintendent	\$264,700 ⁵	163,000	62%
Chief Operations Officer	200,000 ⁶	114,000	75%
Chief Financial Officer	175,000	112,000	56%

In addition to the above salaries, in fiscal year 2004 the district created two Deputy Superintendent positions at \$140,000 each per year. The school district is using data from a compensation study to assist in determining a salary for the new superintendent. The average salary based on this data would rank the superintendent in the top four highest paid in the nation. The district supports the salaries paid to the Chief Operations Officer and Chief Financial Officer with an additional survey, prepared by a human resource consulting firm, of major city education institutions which indicates the salaries paid at the district are in the lower 25th percentile of the national average. The survey results do not appear reasonable since it uses much larger cities, such as Atlanta, San Francisco and New York City, as the basis for its average salaries. Given the current financial condition of the district and comparisons to peer districts, the salaries being paid to these officials do not appear reasonable.

- B. The district's cost of employee health coverage increased 32 percent from \$21.7 million in fiscal year 2001 to \$28.7 million in 2003. In fiscal year 2003, the district employees had the choice of three different health insurance plans, which cost the district between \$373 and \$492 per month per employee. In fiscal year 2004, as a result of joining a group comprised of several other school districts, the district was able to obtain health insurance coverage from a single provider for a lower cost of \$350 per month, per employee, resulting in an estimated savings of \$4 million.

The district has always paid 100 percent of the cost of single coverage health insurance for each employee and required employees to pay the entire cost of family coverage. Due to increasing healthcare costs and the financial position of the district, the administration requested the human resource consultant perform a survey of St. Louis area school districts to compare their benefits to others. The survey indicated employees in other districts are required to contribute an average of 20 percent toward their single coverage insurance but have a portion of family coverage paid by the employer. According to district administrators, requiring a 20 percent contribution (\$70 per month, per employee) for single coverage and

⁵ Average of top nine salaries paid to superintendents from compensation study. Additional incentives/bonuses could also be paid. The prior superintendent was paid \$183,180 for fiscal year 2003.

⁶ The Chief Operations Officer's base salary is \$200,000 annually, plus \$30,000 in possible incentives.

picking up a portion of family coverage would generate an additional \$3 million to be used for district operations.

WE RECOMMEND the School Board:

- A. Perform additional analysis regarding the salaries of its top administrators and ensure such salaries are reasonable.
- B. Continue evaluating options regarding health insurance costs.

AUDITEE'S RESPONSE

- A. *Below is a salary survey prepared in the district using data from the Council of Great City Schools. This information confirms the following:*

Any compensation offer to a new Superintendent for the Saint Louis Public Schools will, of course, be dependent on the candidate's experience, skills, capabilities and fit with the specific requirements of the District. In order to attract an acceptable candidate, it is expected that a total compensation package will have to be competitive with comparable urban school districts like Cleveland, Houston, Fort Worth and Dallas, as shown in the survey material. It is clear that there is a trend in salary escalation for the role of an urban superintendent.

The other positions of Chief Operations Officer and Chief Financial Officer were arrived at using competitive data from the broader public sector, as well as current data from other school districts, since the strategy was to upgrade the skill sets needed for the district and for that reason those new positions were created.

COMPENSATION STUDY - SUPERINTENDENT SEARCH

Data from the Great City Schools indicates the following:

- *In 2003, some 56 percent of Great City Schools superintendents were White; 33 percent were Black; and 10 percent were Hispanic. In 1997 by contrast, 37 percent of Great City Schools Superintendents were White; 47 percent were Black and 16 percent were Hispanic.*
- *As these statistics indicate, the pool of African-American candidates has declined by about 30 percent in six (6) years.*
- *The current average tenure of Great City Schools' superintendents is less than three (3) years while the average tenure of the prior group of superintendents was 4 ³/₄ years. This data suggests that in order to attract and retain a superior candidate for the St. Louis Public Schools, a compensation package needs to be designed in which base pay will be comparable with the best paying urban districts in the*

country, along with a benefits package that is focused on retaining a candidate for the long term.

The current Great City Schools salary data indicates that of the sixty-two (62) urban districts reporting, twenty-one (21) of those have a base salary of at least \$200,000 annually. Of those twenty-one (21) districts, nine (9) of those have a base of over \$235,000 annually, and in that group of nine (9), six of those range in base pay from \$250,000 to \$325,000. Additionally, in those urban districts, bonus pay ranges from \$4,500 to \$100,000.

TOP NINE

Austin	\$236,900
Oakland	\$239,400
Detroit	\$244,800
New York City	\$250,000
Los Angeles	\$250,000
Houston	\$258,000
Cleveland	\$278,000
Fort Worth	\$300,000
Dallas	\$325,000

TOP SIX

New York City	\$250,000
Los Angeles	\$250,000
Houston	\$258,000
Cleveland	\$278,000
Fort Worth	\$300,000
Dallas	\$325,000

- B. *The audit report noted that healthcare cost increased 32% in the last three years in the district. With medical/healthcare inflation currently forecasted to be 12 to 14% over the next three-year period, those past increases, while on the high end, are following general trends nationally. The cost burden of the district is higher than peers because there is no cost for single coverage and the long-term plan will be to shift to a more standard employee cost-sharing model.*

AUDITOR'S COMMENT

- A. The school districts mentioned in this study are not comparable in size to the St. Louis Public School District. The top six districts listed in the study are all significantly larger than St. Louis. The smallest of these schools had approximately 72,000 students, while St. Louis has a total average daily attendance of approximately 39,000 students.

The district's limited approach on its superintendent selection process has caused them to not have a full-time superintendent for the start of fiscal year 2005. The district has appointed an interim superintendent to fill the position.

9. Fixed Assets and Surplus Property

According to the district's independent audit report, movable fixed assets were valued at \$51 million at June 30, 2003. The district does not maintain adequate fixed asset records

and inventories of district property, including surplus property, are not performed. The usage of district owned vehicles has not been evaluated.

- A. The detailed records of the property owned by the district have not been adequately maintained. Fixed asset additions and deletions have not been recorded in the fixed asset records in fiscal year 2004. In addition, although teachers conduct annual physical inventories of the property located in their classrooms, some property in the custody of the administrative and support staff is not inventoried. Also, the district does not reconcile the physical inventories to the fixed asset list.

Property records should be maintained on a perpetual basis, accounting for acquisitions and dispositions as they occur. Complete and accurate property records are necessary to secure better internal control over district property, provide a basis for determining proper insurance coverage, and provide assurance to the public that assets purchased with school monies are being fully utilized by the district. Physical inventories are necessary to ensure the property records are accurate, identify any unreconciled additions, detect theft, and identify any obsolete inventory.

- B. The district currently maintains excessive amounts of surplus property, such as classroom furniture and computer equipment, in its warehouse and at the schools. No inventory listing of surplus property is maintained. We observed the following:

- Property in the 16 closed schools was allowed to be removed by personnel at other schools before an inventory could be taken. The property was relocated to various other locations without any record of what went where.
- Several rooms of the old warehouse contained desks and bookcases piled to the ceiling in an unorganized manner. The old warehouse also contained a significant amount of computer equipment, some usable and some obsolete.
- In excess of 30 pianos in various states of repair were stored in a warehouse.

Since surplus fixed assets are not inventoried, the district has not determined the total value and location of these assets. By keeping an inventory of these items and making all of the schools aware of the surplus property items available, the district can help to ensure any school in need of such property can have access to it. Any unused or obsolete equipment should be disposed of properly.

- C. The district currently maintains numerous vehicles which may no longer be needed for district operations. Many of these vehicles became expendable as a result of the outsourcing of various district operations. For example, the district maintains a total of 32 vans, pickup trucks, and delivery trucks at the buildings and grounds garage, many of which may no longer be necessary due to the

outsourcing of warehouse operations. The district maintains no usage logs for these vehicles and has not performed an assessment to determine the level of usage of these and other vehicles. Allowing unused vehicles to remain in inventory results in unnecessary costs to the district. In addition, the disposal of these vehicles could be used to generate additional funding.

- D. The district maintains ownership of a significant number of unused buildings. Prior to fiscal year 2004, the district did not maintain an official listing of properties for sale and did not actively attempt to sell its surplus real estate. Without an adequate planning function in place, as outlined in MAR 2, the district could not adequately assess the necessity of many of these buildings. During fiscal year 2004, the district established a listing of properties available for sale which included a total of 39 properties with a combined asking price of \$24 million⁷. The list includes 4 vacant lots, 5 office buildings, a greenhouse, 2 houses, 2 warehouses and 25 school buildings. Only one of the 16 recently closed schools (Waring) is included, while the remaining 15 are being evaluated to determine their potential for future use. By allowing many of these buildings to remain unused in the past and to deteriorate, the district will not receive maximum value for the properties.

While no independent appraisals have been performed on any of the district properties listed for sale, the real estate agent did market appraisals and assigned the asking prices to the properties. As of April 19, 2004, the district had sold 6 of the 39 properties on the list at a value of approximately \$2.2 million and had received offers on another 12 properties with a total value of approximately \$2 million. In addition, three properties, including one of the warehouses, have been removed from the for sale list.

The Waring School was valued by the real estate agent at \$1 million and sold for \$1.25 million to the higher of two bids in a public bid process. While the district did not obtain an independent appraisal for the Waring property, the buyer obtained two appraisals that valued the property at \$1.175 million and \$1.21 million.

Obtaining independent appraisals, especially for more marketable properties, would ensure the value assigned is reasonable and represents the fair value of the property.

WE RECOMMEND the School Board:

- A. Maintain property records for all fixed assets and require annual physical inventories of all fixed assets.
- B. Maintain an inventory of surplus property and make a list of surplus property available to the schools. Any unusable items should be disposed of properly.

⁷ Includes the main administrative building with an asking price of \$10,000,000.

- C. Make a determination of its fleet usage and needs and dispose of any unneeded vehicles in inventory.
- D. Continue efforts to identify any unnecessary surplus properties and attempt to dispose of them. The Board should consider obtaining an independent real estate appraisal on any marketable surplus real estate prior to putting the property up for sale to ensure the district receives the maximum value for the property.

AUDITEE'S RESPONSE

We agree with the recommendations.

- A. *Existing records were out-of-date and incomplete. As a result of staff reductions, the property records for fixed assets have not been brought up to date to reflect the significant changes that have taken place in terms of closed facilities, recognition of obsolete inventory and unneeded assets and the overall down-sizing of the District.*
- B. *An inventory of usable surplus property and equipment is being compiled and will be made available to the schools once it is completed. It is estimated that this will be complete **September 2004**.*

Inventory and equipment from closed facilities (both those recently closed and those on the market for sale) are now being reviewed for usefulness and equipment considered obsolete or unusable is being disposed of.

The district is also reviewing procedures necessary to implement physical inventories at all major sites.

- C. *A review of the fleet is being conducted and any unneeded vehicles will be disposed of by **August 2004**.*
- D. *We continue to market the surplus properties in an effort to raise additional cash for the district. In the initial efforts to market the first 39 surplus properties, it was felt that it was adequate to use market comparable comparisons to set prices for the properties to be sold, rather than accepting the delays and costs of obtaining formal appraisals for the buildings. In the case of the Waring School, the price set in this way was close to the formal appraisal carried out by the ultimate buyer.*

10.	Board Minutes, Meetings, and Policies
------------	--

The School Board was not preparing meeting minutes with an adequate level of detail and these minutes were sometimes not prepared and approved in a timely manner. Several problems were also noted regarding the Board's closed meetings and related minutes.

- A. The minutes of the open public meetings did not adequately or clearly document all items discussed or decisions made by the Board. For example, minutes documented the fact that the fiscal year 2003 and 2004 budgets had been approved and included the budget figures, but contained no documentation of discussions related to the development of the budget. In addition, the fiscal year 2003 management letter from the district's independent auditor noted that minutes from recent school board meetings were not prepared, approved, and made available for review in a timely manner.

The minutes are the only official record of the action of the board. Care should be taken to ensure the minutes are complete and document discussions and specific intentions or reasons behind board decisions. Inadequate or unclear minutes can lead to subsequent confusion as to the board's intentions and possible incorrect interpretation of the board's actions by the general public or other outside entities.

- B. The School Board did not always document how some items discussed in closed session complied with state law. Section 610.021, RSMo 2000, allows matters to be discussed in closed session only if they relate to certain specified subjects. Those subjects that would appear to be most applicable to the school board include matters related to pending or possible litigation, real estate transactions, and personnel actions involving specific employees.

Closed session meeting minutes documented discussions on topics related to budgetary and financial condition matters which do not appear to be allowable topics. To ensure compliance with the state law, care should be taken to ensure only matters specifically authorized by law are discussed in closed session.

- C. The School Board did not always document the roll call vote to open a closed session meeting as required by 610.022, RSMo 2000, nor did they always document the roll call of a vote taken during closed session as required by 610.015, RSMo 2000. Additionally, minutes were not prepared for some closed session meetings and, in cases where minutes were prepared, the Board President did not approve them.

Although state law does not require public bodies to record minutes of closed meetings/sessions, state law puts the burden on public bodies to demonstrate compliance with all Sunshine Law provisions.

- D. District policies and regulations concerning cash operations, records, and controls at the school level have not been updated and effectively communicated to the building administrators. Although the district's internal reviews of cash reference several policies in this area, the current district manual, including the one posted on the district's website, does not include these policies. Properly communicated policies and procedures provide a framework for their effective implementation.

WE RECOMMEND the School Board:

- A. Ensure minutes from all meetings of the board provide adequate and clear details of the issues discussed.
- B. Ensure only matters specifically authorized by law are discussed in closed session.
- C. Ensure closed session board minutes are signed by the Board President, that minutes are maintained for all closed meetings, and that roll call votes are taken and documented for opening closed session meetings, as well as for votes made during closed session.
- D. Ensure policies and procedures manuals are kept up to date and such policies are communicated to the applicable personnel responsible for implementation and monitoring.

AUDITEE'S RESPONSE

The Board of Education has restructured the Board Office. New personnel have been assigned to the office to ensure proper record keeping and efficient day-to-day operations in the Board Office. The staff has familiarized themselves with the relevant statutes and bylaws governing the school board.

- A. *The Board and staff are preparing formalized guidelines for the preparation of minutes. These guidelines will be presented to the Board for approval. The minutes are now prepared and presented to the Board for approval prior to the subsequent monthly meeting.*
- B. *The Board Office personnel have developed and implemented a plan of consultation and review of all items being considered for the closed session agenda. All items placed on the closed session agenda are reviewed and approved by a board attorney. The specific subsection of the §610.021 RSMo 2000 that applies is identified and a recommendation is made to the Board President who makes the final determination. Only items which meet the exception set forth in §610.021 RSMo 2000 are allowed. The new formalized guidelines for minutes will require that the rationale for items considered in closed session be included in the record.*
- C. *The Board is currently in compliance with §610.022 RSMo 2000, which requires that all business conducted in closed and open session be recorded by a roll call vote. The roll call votes are recorded on a standardized roll call vote form. Executive session minutes are prepared by the Board staff, reviewed and signed by the Board President. The Board demonstrates Sunshine Law compliance in its closed session meetings by reporting to the public any actions taken within the 72 hours.*

- D. *The Board is in the process of establishing a Policy and Regulations Committee that will engage in a comprehensive revision of the existing Policies and Regulations in order to create continuity in the context of the new organizational structure, which has been created in the district. The Committee will make recommendations to the Board for approval. The newly adopted policies will be communicated to the staff at the Board Office and School levels through publication and department meetings.*

11. Internal Audit

The district does not have an internal audit section or position. Internal audits can be a valuable management tool by identifying ineffective or inefficient operations and ensuring that established policies and procedures are followed. A district of this size and complexity should consider an independent internal audit function to ensure compliance with operating regulations and to provide assurances that maximum use of resources is being made. A properly functioning internal audit section could have helped in discovering and resolving several of the areas commented on in this report including school planning, food service, contract management, budgeting, transportation, warehouse operations, fixed asset management, and travel policies and expenses. An internal audit section could also audit and monitor compliance with new service contracts.

The district has performed a limited number of cash reviews in the past; however, the number of these reviews has been reduced in recent years. Past reviews have noted several control deficiencies in the school level cash functions that need to be followed up to ensure the monies are used for their intended purposes.

The need for an internal audit function was also noted by the district's independent audit report.

WE RECOMMEND the School Board consider establishing an internal audit section.

AUDITEE'S RESPONSE

The District has reinstituted an internal audit function through the Fiscal Control Department conducting audits at the school level in terms of cash receipt, control and deposit and record-keeping. A regularly scheduled set of school audits will be conducted, with follow up reporting and required corrections where identified.

In view of further personnel reductions that are anticipated as a part of the cost reductions necessary to bring overall expenses into line with revenues, the plan is not to expand the current level of internal audits. The revised financial reporting, that was discussed in Section 4, should provide greater visibility and analysis to many of the areas referred to in this report that led to the unanticipated financial shortfalls and surprises in the 2003 fiscal year.

**3222 Hawthorne Blvd.
St. Louis, MO 63104
May 23, 2004**

**Honorable Claire McCaskill
1015 Locust, Suite 510
St. Louis, MO 63101**

Dear Honorable McCaskill:

Again I appreciate the opportunity to respond to a draft of your report. I am told that your examination is being called a performance audit. It would be helpful if you were to define what a performance audit is and is not.

My first concern is the scope of your examination of the food service operation. After a long history of an efficient and effective department, you only examined the last two lean budget years. It is not uncommon for school systems to subsidize lunch programs. Student lunch programs were never intended as a profit maker. The change to a private company has meant the loss of many local jobs without any assurance that the quality will be maintained.

The second concern is the mystery around records and reports that can not be found. The best example is transportation where annual public reports were made to the board of education, but no record can be found. Action was taken on the reports including the reassignment of routes.

The research department headed by Dr. Ron Mertz evaluated a number of programs including the motivational program that you mentioned in your report. A simple telephone call to Dr. Mertz could have cleared up the matter.

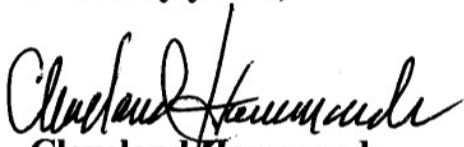
Your chart and comments comparing spending in St. Louis and other cities did not follow good research procedures. No effort was made to make sure the definitions were the same. There was no explanation of instruction and what that category contained. What purpose did it serve but to strengthen the myth about waste in the system?

No attempt was made to capture the full cost of administration including all of the consultants hired during the current year. Did all of the contracts have goals and how were they measured?

In summary, the deficit was caused by state cuts, the disputed desegregation funds, cost of the charter schools and cost of the teachers' contract. We thought we would only have to cover the cost of the teachers' contract with our reserve as a worse case scenario. No one anywhere had predicted the state and national budget crisis. Part of the system's budget balance came because of good economic times, but a significant part of it was gained through good management. The firm was not hired because of the deficit. They were contracted before the board or anyone else knew of the extent of the problem. I maintain that the board got what information that was available.

You faced a difficult challenge trying to judge the operation of a large complex organization in a year. You have made a good start, however, the impact of many of the recent changes cannot be known yet.

Sincerely yours,


Cleveland Hammonds

HISTORY, ORGANIZATION, AND
STATISTICAL INFORMATION

REVIEW OF THE ST LOUIS PUBLIC SCHOOL DISTRICT HISTORY AND ORGANIZATION

The St. Louis Public School District encompasses the entire city of St. Louis, Missouri, approximately 61 square miles, and serves a population of approximately 339,000 citizens. With a total average daily attendance of approximately 39,000 students in school year 2002-2003 and total budgeted general operating expenditures historically exceeding \$380 million per year, the district operates as the largest public school system in the State of Missouri. As of June 30, 2003, the district employed approximately 6,570 individuals, including approximately 4,100 full-time teachers and certified personnel.

Prior to the 2003-2004 school year the district operated 109 schools as follows: four regular high schools (9-12), five magnet high schools, fifteen regular middle schools (6-8), seven magnet middle schools, fifty-seven regular elementary schools (K-5), fifteen magnet elementary schools, two alternative high schools, one alternative middle school, and three special schools. In the summer of 2003, the district closed a total of 16 schools; twelve regular elementary schools, one magnet elementary school, one regular middle school, one alternative high school and the alternative middle school. The district now operates a total of 93 schools.

The St. Louis Public School District has been classified under the Missouri School Improvement Program (MSIP) as "Provisionally Accredited" by the Missouri Department of Elementary and Secondary Education (DESE). A provisionally accredited district has not met enough of the MSIP standards and indicators to be accredited but has shown some improvement over time. In addition, the St. Louis Public School District has been classified as "financially stressed." Section 161.520, RSMo 2000, considers a district to be "financially stressed" if the year end operating funds balance is less than three percent of expenditures or is negative.

An elected board acts as the policy-making body for the district's operations. The board's seven members serve 3-year terms without compensation. Four new members were elected to the board in April 2003, while two of the remaining three members have served since 2001 and one has served since April 1997. Members of the board during the year ended June 30, 2003, were:

Name and Position	Term
Darnetta Clinkscale, President	April 2003 to April 2007
William R. Purdy, President	April 1991 to April 2003
Ronald L. Jackson, Vice President	April 2003 to April 2007
Harold M. Brewster, Vice President	April 1997 to April 2003
Dr. Amy L. Hilgemann, Secretary	April 2001 to April 2005
Robert Archibald, Member	April 2003 to April 2007
Paulette McKinney, Secretary	April 1999 to April 2003
William C. Haas, Member	April 1997 to April 2005
Rochell Moore, Member (1)	April 2001 to April 2005
Vincent C. Schoemehl, Jr., Member	April 2003 to April 2006
Marlene E. Davis, Member	April 1997 to April 2003

- (1) Removed from the Board in May 2004. Veronica O'Brien was appointed to the position in May 2004.

The district's other principal officials during the year ended June 30, 2003, are identified below. The compensation of these officials was established by the school board.

<u>Central Administration 2002-03</u>	<u>Annual Compensation</u>
Dr. Cleveland Hammonds, Jr. Superintendent (2)	\$ 183,180
Mulegheta Teferi, Chief Academic Officer (3)	110,000
Chester Edmonds, Executive Assistant – Operations (4)	105,000
Dr. Charlene Jones, Assistant Superintendent over MSIP	91,302
Ida Woolfolk, Assistant to Superintendent for Community Outreach (5)	79,567
David Flieg, Executive Assistant for Administration	86,005
Dr. Charles L. Hutchins, Senior Advisor, Evaluation, Research and Assessment	101,623
George Byron, Treasurer (4)	81,149
Dori Freelain, Fiscal Control Officer (4)	86,945
Wayne Fisher, Building Commissioner (6)	95,000
Charles Pineau, Director of Human Resources	85,000
Linda Riekes, Development Officer	71,056
Charles McCrary, Director of Security	81,075
Mayde Henson, Lead Initiative Project Director (7)	100,000

- (2) Retired June 30, 2003.
- (3) Reassigned as principal of Gateway Middle School August 4, 2003.
- (4) Resigned August 14, 2003.

- (5) Retired September 1, 2003.
- (6) Terminated January 31, 2004.
- (7) Contracted employee. This contract was not renewed for 2004.

In January 2003, the Prior Superintendent, Dr. Cleveland Hammonds, announced his retirement effective at the end of fiscal year 2003. After the April 2003 election, the new Board voted in May 2003 to hire a management services firm (management team), Alvarez and Marsal, to take over district operations starting in July 2003. In addition, the district hired a performance audit firm or consultant, McConnell, Jones, Lanier, and Murphy, LLP (MJLM). During the 2003-2004 fiscal year, many changes occurred in the organization of district management as well as in management personnel. The organizational charts for fiscal years 2003 and 2004 included in the following pages show the changes in the organizational structure of the district.

The principal officials and their revised titles as of March 31, 2004, are listed below.

<u>Central Administration 2003-04</u>	<u>Annual Compensation</u>
William V. Roberti, Acting Superintendent	(8)
Manuel Silva, Chief Operating Officer/ Building Commissioner (9)	\$200,000
Harry Rich, Chief Financial Officer (10)	175,000
Floyd Crues, Deputy Superintendent, Middle and Secondary Schools, Alternative and Special Education (11)	140,000
David Flieg, Deputy Superintendent, Elementary Schools and Title I (11)	140,000
Dr. Charles L. Hutchins, Assistant Superintendent, Research, Accountability, Assessment and Development	110,000
Dr. Charlene Jones, Assistant Superintendent, Institutional Relations	91,302
Charles McCrary, Director of Security	81,075

- (8) Contracted member of the Alvarez & Marsal management team since June 2003, billed per contract at a rate of \$425 per hour (2,194 hours through April 2004.) In June 2004, Floyd Crues was appointed interim superintendent until a permanent superintendent can be hired.
- (9) Hired December 3, 2003. Karen Marsal, contracted member of Alvarez & Marsal management team, was the Interim Chief Operating Officer from June 2003 until Mr. Silva's hire. Mr. Silva's compensation package includes an additional \$30,000 in incentives for completing certain job tasks. Ms. Marsal was billed per contract at a rate of \$325 per hour (1,907 hours through April 2004.)

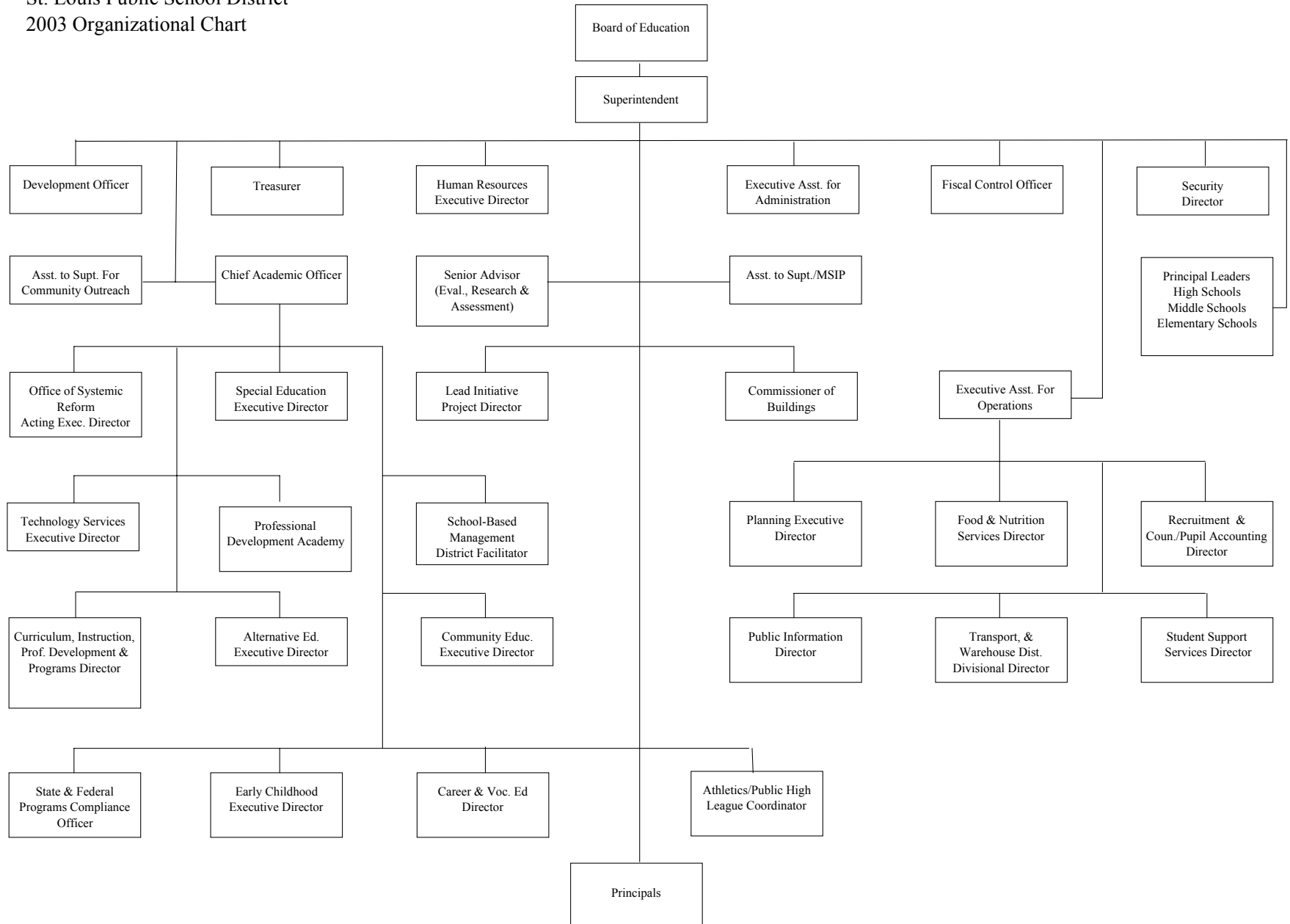
(10) Hired November 5, 2003. Sajan George, contracted member of Alvarez & Marsal management team, was the Interim Chief Financial Officer from June 2003 until Mr. Rich's hire. Mr. George was billed per contract at a rate of \$375 per hour (1,954 hours through April 2004.)

(11) Promoted to position in November 2003.

Assessed valuations and tax rates for 2003 and 2002 were as follows:

	2003	2002
Assessed valuation	\$ <u>3,332,578,940</u>	<u>3,161,745,493</u>
Tax rates:		
Incidental	\$ 3.640	3.750
Debt service	<u>.550</u>	<u>.550</u>
Total	\$ <u>4.190</u>	<u>4.300</u>

St. Louis Public School District
2003 Organizational Chart



St. Louis Public School District
2004 Organizational Chart

